

In computing Retailers' Occupation Tax liability, no deductions shall be taken by a taxpayer from gross receipts on account of the cost of the property sold, the cost of materials used, labor costs, or any other expense whatsoever. See 86 Ill. Adm. Code 130.410. (This is a GIL.)

November 8, 2000

Dear Xxxxx:

This letter is in response to your letter dated July 7, 2000 that we received on July 27, 2000. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be accessed at the Department's Website at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter, you have stated and made inquiry as follows:

We are requesting an opinion for a taxpayer on the following sales tax issues that we are trying to resolve. The taxpayer is a job shop that makes a wide variety of fabricated steel products. The taxpayer would like some direction on the correct way to handle the sales tax incurred when they sell these items. Listed below are a few examples of products/services that they provide and some related questions:

1.) Railings

The taxpayer designs and fabricates hand, wall, and balcony railing. Each railing that they fabricate is a special-order railing in that it is designed to match the slope and shape of the sidewalk/staircase/etc. that it will go around. Each railing is unique from all other railings. The railing would not have value to any other purchaser because it is made to the specifications of the property that it will be installed on. Is this type of work subject to the SOT or ROT? Also, when the railing is finished, the customer usually does the installation. At times though, the taxpayer installs the railings. What sales tax effect would it have if the taxpayer had a separate contract to do the installation vs. if the installation was a part of the contract for the railings?

2.) Structural Steel Jobs

In another area of the taxpayer's business, they supply structural steel for contractors. They supply I-beams, channel iron, angle iron, etc. At times, they will simply be a steel supplier in which case the taxpayer charges ROT on the

selling price of the steel. Most of the time though, they custom make the beam to the buyer's specifications. This usually means that they cut the beams, drill holes in the beams, weld on the beams, etc. Oftentimes, this will make the beam useless to anyone other than the purchaser (because of the hole pattern, added components to the I-beams, etc.). In essence, when the taxpayer does extra work to the beams to meet the customer's specifications, they are providing them a service. Can the taxpayer look at this transaction as one that would be subject to SOT and bill tax on the steel, but not on the labor?

3.) Cutting Jobs

The taxpayer uses a plasma/torch machine and a laser cutting system to cut steel. The work done on these machines is billed out according to the amount of time that it takes for the machine to cut the material. On most of the jobs, they furnish the material as well as the service of cutting. The pieces that they cut for customers are usually one-of-a-kind parts. They do on occasion, make the same parts over and over for the same customer. When they operate these machines is the taxpayer providing a service with material adjacent to the service or are they providing a product at retail that is subject to ROT? Is it significant that some parts that they cut are repeated and not a one-time run?

4.) Miscellaneous Custom Fabrications

Like all job shops, the taxpayer custom fabricate a large variety of products that do not fit into the categories described above. By custom fabrication, we are referring to making unique products of all sorts. An example of a few of these products would be steel ramps, platforms, and stair pans. These items are made specifically to the customer's specifications and are unique to the customer. Usually, these items will have no value to anyone other than the purchaser. They would have no value to the purchaser except for the result of the service the taxpayer performs (forming, punching, welding, cutting, etc.). The customers come to the taxpayer because of their special expertise in custom fabrications. Are these one-of-a-kind products subject to the SOT with tax on the material portion of the order only, or are these products considered TPP that is subject to the ROT?

5.) Work performed on Trucks/Trailers

Occasionally, the taxpayer will install hitches, steel metal, etc. on trucks and trailers. They have been told that whenever they add something permanent to a truck or a trailer then tax must be charged on the entire sales amount. Is this correct? Are there specific sections in the Adm. Code that address this?

6.) Manufacturing Machinery & Equipment Exemption

Section 130.330(Product Use) of the Illinois Dept. of Revenue Code describes a scenario in which machinery & equipment used in the performance of a **service** may be non-taxable if they are used to produce goods for sale or lease as a result of the service. The taxpayer would like to know if the machinery that they

purchase is considered exempt MM & E. In the past, the taxpayer has purchased machinery and equipment for use in the following scenarios:

1. End users provide the taxpayer with their tangible personal property (TPP) and request that the taxpayer change the TPP by welding, cutting, drilling, bending, etc. They perform these services to the customer and then return the modified TPP to the customer.
2. Resellers (agriculture and heavy equipment manufacturers) provide the taxpayer with parts or sub-components, and the taxpayer uses their machinery and equipment to alter the parts and then return them to the manufacturers. An example of this would be production welding on agriculture implements.

Due to the nature of the taxpayer, their machinery is typically used to perform both of these types of services. However, these machines are used more than 50% of the time on production-type work for their customers who are resellers.

Any advice or clarification that you can give on these issues will be sincerely appreciated. If you need additional information, please contact me at #####.

We do not have sufficient information about the sales of the railings in order to make a determination about their tax status. You state the taxpayer designs the railings according to customer specifications and that the railings have value only to the particular purchaser who usually, although not always, does the installation. Please note that certain building material items made to order and sold without installation by the seller as a construction contractor are considered retail sales because such items, even though produced on special order, serve substantially the same function as stock or standard items of tangible personal property sold at retail. Such items can include screen doors, storm doors, window screens, and awnings. See 86 Ill. Adm. Code 130.2140, enclosed. If, however, taxpayer's design function in production of the railings were such that their sales were service transactions, they would be subject to liability under the Service Occupation Tax Act. Please refer to 86 Ill. Adm. Code 130.2115 and 140.101, enclosed.

If the taxpayer were to permanently affix the railings to real estate, the taxpayer would act as a construction contractor and, as such, would incur a Use Tax liability on his cost price of the materials permanently affixed to real estate. There would be no tax incurred by the customer. There would be no tax due upon any installation charge in these circumstances. See 86 Ill. Adm. Code 130.1940, enclosed.

From the limited amount of information provided, we believe that sales of the steel platforms, I-beams, channel iron and other steel products described in paragraphs 2, 3, and 4 of your letter are sales at retail subject to the Retailers' Occupation Tax Act. We believe these transactions are governed by the Illinois Supreme Court's decision in the case of Sterling Steel Casting Company v. Department of Revenue, 7 Ill. 2d 244 (1955). In Sterling the taxpayer, a steel manufacturer who made steel castings from patterns furnished by its customers, argued that it was engaged in a service occupation for the steel castings it made upon special order for customers. Taxpayer made this argument upon the basis the special order castings were only usable by the particular customers who ordered them and that they had no purpose other than that for which they were ordered.

The Supreme Court disagreed with taxpayer and held the transactions to be retail sales subject to liability under the Retailers' Occupation Tax Act. The court noted that taxpayer was not primarily engaged in furnishing technical engineering service apart from its general "know how." The court further noted that taxpayer was engaged in the business of producing and selling tangible personal property at retail, in which the element of service was incidental, Sterling at 250.

Regarding the retail sale of hitches, sheet metal or other tangible personal property that is installed upon trailers or trucks, the seller would incur Retailers' Occupation Tax liability based upon his total gross receipts. In computing Retailers' Occupation Tax liability, no deductions shall be taken by a taxpayer from gross receipts on account of the cost of the property sold, the cost of materials used, labor costs, or any other expense whatsoever. See 86 Ill. Adm. Code 130.410, enclosed.

Enclosed is a copy of 86 Ill. Adm. Code 130.330 concerning the Manufacturing Machinery and Equipment Exemption. In general, the Retailers' Occupation Tax does not apply to sales of machinery and equipment used primarily in the manufacturing or assembling of tangible personal property for wholesale or retail sale or lease.

When determining whether a piece of equipment qualifies for the manufacturing machinery and equipment exemption, the requirements of 86 Ill. Adm. Code 130.330 must be met. This regulation describes the manufacturing process as the production of articles of tangible personal property or the assembling of different articles of tangible personal property by procedures commonly regarded as manufacturing, processing, fabricating, or refining which changes some existing material or materials into a material with a different form, use or name. These changes must result from the process in question and be substantial and significant, Section 130.330(b)(2).

In general, machinery or equipment used in the performance of a service is not used in the production of tangible personal property for sale and thus is taxable upon purchase, 86 Ill. Adm. Code 130.330(e)(3). However, please note the same subsection explains that a manufacturer who uses machinery or equipment to produce goods for sale or lease by himself or another, or to perform assembly or fabricating work for a customer who retains the manufacturer only for his services, will not be liable for tax on the machinery or equipment he uses as long as the goods produced either for himself or another are destined for sale or lease, rather than for use or consumption.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

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Associate Counsel

KWB:msk
Enc.